VZCZCXRO4604
RR RUEHAST RUEHBI RUEHCI RUEHLH RUEHNEH RUEHPW
DE RUEHNE #3138/01 3471014
ZNR UUUUU ZZH
R 121014Z DEC 08
FM AMEMBASSY NEW DELHI
TO RUEHC/SECSTATE WASHDC 4678
INFO RUCNCLS/ALL SOUTH AND CENTRAL ASIA COLLECTIVE
RUCPDOC/DEPT OF COMMERCE WASHDC
RHEBAAA/DEPT OF ENERGY WASHDC
RUEATRS/DEPT OF TREASURY WASHDC
RULSDMK/DEPT OF TRANSPORTATION WASHDC
RHMFIUU/FAA NATIONAL HQ WASHINGTON DC
RUEHRC/DEPT OF AGRICULTURE WASHDC

UNCLAS SECTION 01 OF 04 NEW DELHI 003138

SIPDIS
SENSITIVE

STATE FOR SCA/INS AND EEB
USDOC FOR ITA/MAC/OSA/LDROKER/ASTERN/KRUDD
DEPT OF ENERGY FOR A/S KHARBERT, TCUTLER, CZAMUDA, RLUHAR
DEPT PASS TO USTR CLILIENFELD/AADLER/CHINCKLEY
DEPT PASS TO TREASURY FOR OFFICE OF SOUTH ASIA MNUGENT
TREASURY PASS TO FRB SAN FRANCISCO/TERESA CURRAN
USDA PASS FAS/OCRA/RADLER/BEAN/CARVER/RIKER
EEB/CIP DAS GROSS, FSAEED, MSELINGER

E.O. 12958: N/A
TAGS: EAGR EAIR ECON ECPS EFIN EINV EMIN ENRG EPET ETRD
BEXP, KIPR, KWMN, PHUM, SENV, ASEC, KFLU, IN

SUBJECT: NEW DELHI WEEKLY ECON OFFICE HIGHLIGHTS FOR THE WEEK OF
DECEMBER 8 TO DECEMBER 12, 2008

¶1. (U) Below is a compilation of economic highlights from Embassy New Delhi for the week of December 8 to December 12, 2008, including the following:

-- Macro Update
-- Speculation on New Finance Minister
-- World Bank to Address Infrastructure and Poverty
-- India's Infrastructure Registers Sluggish Growth
-- GOI Allows Fertilizer Companies to Issue Fertilizer Bonds
-- India to Go Slow on Bilateral Trade Plans with Pakistan
-- Renault Scales Down Chennai Facility
-- Tamil Nadu Changing Policies on Electricity Sales

Macro Update

¶2. (U) Economic outlook for India deteriorates with World Bank & Morgan Stanley further downgrading India's growth forecasts (5.8% for 2009 & 5.3% for FY09 respectively). A blend of monetary and fiscal measures were announced, like policy rate cuts (1% reduction in Repo and Reverse Repo rates), excise duty cuts (across the board 4% excise duty cut barring petroleum products) and increased government outlays (USD 4 bn), to combat the decelerating growth momentum. The fiscal package drew a mixed response from industry with some sectors like construction and real estate expecting a bigger boost. In addition, the government permitted IIFCL to raise tax free bonds to the tune of USD 2 bn, to facilitate financial closure for infrastructure projects under the PPP route. The government is also taking steps to ensure that the already budgeted expenditure of USD 60 bn is actually spent over the next four months of the current fiscal year. The recent fiscal stimulus package of approximately 0.6% of GDP will imply a further slippage in the deficit figures. Inflation rate fell further to a seven month low of 8% (Nov 29) mainly on account of easing food prices.

Speculation on New Finance Minister

¶3. (SBU) Press reported this week on possible replacements for Chidambaram, who became Home Minister following the November 26 Mumbai terrorist attack, as Minister of Finance. Names being considered include former Karnataka Chief Minister SM Krishna, Union

Commerce and Industry Minister Kamal Nath, Rajya Sabha Member and Former Reserve Bank of India Governor C Rangarajan, and Deputy Chairman of the Planning Commission, Montek Singh Ahulwalia. Some Econoff contacts suggest that the most likely of the four is Rangarajan because the Ministry needs someone well-versed in finance to manage the daily flow of issues and decision-making, especially during the ongoing financial and economic slowdown. The other most likely possibility is that no one is named before national elections, in which case Montek Ahluwalia will de facto run MOF, reporting directly to the Prime Minister as he does now in the Planning Commission.

¶4. (SBU) SM Krishna, (76 years old) may be favored because of his political credentials. Krishna, a lawyer by profession has held many prestigious positions such as former Governor of Maharashtra and former Chief Minister of Karnataka. Krishna resigned as Governor of Maharashtra on March 5, 2008 in order to return to active politics in Karnataka. Kamal Nath, (62 years old) Union Commerce and Industry Minister, appointed since May 2004 has earlier served in various ministerial capacities including as Union Minister of State for the Environment and Forests and Textiles. Nath has witnessed major trade policy initiatives as Minister of Commerce and Industry. (Comment: One contact theorized that Nath may be generally discredited in Congress party circles for having promised a definitive win in his home state of Madhya Pradesh, which did not happen. End comment.) Dr. C. Rangarajan (76 years old), who recently became a Rajya Sabha Member, is a leading economist who has played a key role as a policy maker. He has held several important positions including as Chairman of Prime Minister Manmohan Singh's Economic Advisory Council, Governor of Reserve Bank of India and Governor of Andhra Pradesh. Rangarajan may be Prime Minister Singh's

choice because of his vast technocratic experience. Montek Singh Ahluwalia (65 years old) has been the Deputy Chairman of the Planning Commission since June 2004 and is considered a close economic advisor to the Prime Minister. He is not a member of Parliament could hold the office for six months without being a member of either house. He was Finance Secretary in Manmohan Singh's team in the Finance Ministry, which initiated economic reforms in the early 1990s.

World Bank to Address Infrastructure and Poverty

¶5. (U) The Wnrld Bank on December 11 released India's Country Strategy for the years 2009-12, anticipating total lending of $14 billion over the next three years, of which $9.6 billion will be from the International Bank for Reconstruction and Development (IBRD) and $4.4 billion from the concessional International Development Association (IDA). The strategy aims to fast-track the development of much-needed infrastructure and to support the seven poorest states (Bihar, Chhattisgarh, Jharkhand, Madhya Pradesh, Orissa, Rajasthan, and Uttar Pradesh) in achieving higher standards of living for their people. World Bank's Economic Adviser Giovanna Prennushi argues that in order to sustain India's rapid growth, it needs to include the 300 million people who live below the poverty line. India's vast infrastructure deficits also need to be addressed as no Indian city provides water 24 hours a day and only half the population has access to safe drinking water. About 40 percent of India's 600,000 villages are not connected to a road. India was the largest IDA and second largest IBRD borrower from the Bank in 2008.

India's Infrastructure Registers Sluggish Growth

¶6. (SBU) India's infrastructure sector, with a combined weight of 26.7 percent in the index of industrial production (IIP), slowed to 3.4 percent growth in October 2008 versus 4.8 percent in the previous month and 4.6 percent in October 2007. The core sector has been posting weak growth throughout the fiscal year. Cumulative core sector growth for April-October 2008 was just 3.9 percent as compared to 6.6 percent registered during the corresponding period of last year. The steel sector was the worst hit, registering a negative growth of 0.5 percent against 5.2 percent in October 2007,

due to a slowdown in demand and a sharp downturn in steel prices. Electricity production remained flat at 4.4 percent. However, coal output was up by 10.9 percent in October 2008 vis-`-vis 8.9 percent in the previous year. Output of petroleum products nearly doubled to 5 percent from 2.7 percent. Cement output grew by a healthy 6.2 percent in October 2008, with cement inventories at wholesalers increasing.

¶7. (SBU) This week, in order to make more funds available to the infrastructure sector, the government approved the issuance of tax free bonds totaling $2 billion (Rs 100 billion) by the state-owned India Infrastructure Finance Company (IIFCL). The IIFCL will raise the funds through a combination of private placement and public issue. The coupon rate for the proposed bonds will be 7.5 percent. IIFCL will lend the funds to banks for refinancing infrastructure projects, particularly in the road and ports sector, at 8.5 percent. IIFCL will also lend directly through consortium-lending sources. The government is expected to invite bids for over 50 highway projects worth $10 billion (Rs 500 billion).

GOI Allows Fertilizer Companies to Issue Fertilizer Bonds
--- ----

¶8. (SBU) The Finance Ministry on December 10 gave permission to 23 government-owned fertilizer companies to issue special bonds worth $2 billion (Rs 100 billion) as compensation towards the fertilizer subsidy during FY 2008-09. The largest subsidy ($596 million) is being given to Indian Farmers Fertilizer Co-operative Ltd followed by Coromandal Fertilizers Ltd ($230 million) and Indian Potash Ltd ($219 million) to help these firms meet their working capital

requirements. The 14-year bonds are being issued at the coupon rate of 7 percent. These bonds will not be eligible as statutory requirements of banks for investment in government securities. However, the investment by the provident funds, gratuity funds and superannuation funds in the bonds will be treated as an eligible investment. Banks will be allowed to sell these bonds to the Reserve Bank of India whenever they want, thus ensuring liquidity of these bonds. The government received approval for reimbursing fertilizer companies for the cost of the controlled fertilizer prices for $7.8 billion (Rs 389 billion) by way of cash outgo and $2.8 billion (Rs 140 billion) through bonds in the supplemental budget passed in October. With global crude prices now coming down, the fertilizer subsidy may also be lower. Analysts point out that the fertilizer companies wanted to receive the subsidy in cash rather than through bonds, because they had to sell them at a 15 percent discount last fiscal year.

India to Go Slow on Bilateral Trade Plans with Pakistan
--- ------

¶9. (U) Last month's Mumbai terror attack will likely affect nascent trade openings between the two countries going forward. Minister of State for Commerce Jairam Ramesh has reportedly said that in the aftermath of the attacks, no new initiatives will be started and India will have to revisit trade plans with Pakistan. India and Pakistan, in September 2008, took steps to promote bilateral trade despite the traditional sensitivities involved between the two countries. India's trade plan included removing Pakistan from the list of countries from where foreign direct investment was not allowed due to security reasons; opening two branches of commercial banks of India and Pakistan on a reciprocal basis; permitting trade in several hundred items compared with the current 13 across the Attari-Wagah border and the Khokrapar-Munabao border; and opening the Skardu-Kargil route in Jammu and Kashmir for commerce. The Indian government has also dropped a plan to launch a website containing specific details of procedures to be followed by Pakistani exporters aiming to trade with India.

¶10. (U) Immediately after the Mumbai attacks, India abandoned plans to set up border posts to facilitate movement of goods and people to and from Pakistan, Bangladesh, Nepal and Myanmar. However, India will continue to allow trade across the Line of Control in Jammu and Kashmir, which is restricted to 21 items including fresh and dry fruits, spices, honey, leather slippers, walnut-wood furniture, wall

hangings, embroidery items, tamarind, green gram, carpets, shawls, black mushrooms, pillows and pillow covers, medicinal plants, rice, blankets, rugs, woolen garments, saffron and kadam, a vegetable.

¶11. (U) Bilateral legal trade between India and Pakistan increased to $2.3 billion in 2007-08 (0.5 percent of India's total trade turnover) from $345 million in 2003-04. According to some trade observers, suspension of trade ties has more of an impact for Pakistan than for India, given Pakistan's minimal share in India's trade.

Renault Scales Down Chennai Facility

¶12. (SBU) Carmaker Renault-Nissan announced on December 9 a scaling down of its plans to manufacture automobiles in Chennai. The company is currently building a plant -- due to open in 2009 -- that was originally supposed to produce up to 500,000 cars per year. A company spokesman told Consulate General Chennai that the plant will now operate only one line and produce only two types of sub-compact cars developed for the Indian market, which should be available to consumers in 2010. He said that Renault-Nissan had dropped plans to produce a larger sedan at the facility because a key supplier withdrew from an agreement to provide critical components for the project. A journalist from a leading business daily told us, however, that Renault-Nissan dropped its sedan plans because larger cars are selling extremely poorly in India.

Tamil Nadu Changing Policies on Electricity Sales

--- ----

¶13. (SBU) Still reeling from electricity shortfalls, the state of Tamil Nadu continues to shift policy on sales of power by private producers to encourage greater use of as-yet untapped sources of electricity generation. The Tamil Nadu Electricity Regulatory Commission (TNERC) has hitherto required that private producers of electricity (i.e., producers other than the Tamil Nadu Electricity Board, TNEB) pay a "cross-subsidy surcharge" to TNEB. The purpose of this fee was ostensibly to help TNEB compensate for potential lost revenues required to achieve its "social goals," which include below-cost power to most individual consumers and free power to farmers. (Consulate General Chennai hears frequent complaints from companies that farmers tend to sell this electricity rather than use it to irrigate crops.) The actual effect was to discourage potential private producers from generating electricity for sale to power-starved industries.

¶14. (U) The TNERC will now allow the TNEB to drop the surcharge requirement. This move, championed by the Confederation of Indian Industry (CII) and other business groups, should increase the incentive for private producers to sell power. CII argued that many companies in the state have installed back-up generators that could be used to generate electricity for sale to other companies, particularly in the current economic climate, when many manufacturers are seeing orders for their products plummet. The chairman of a Coimbatore-based textile company told us that his facility has installed back-up generation capacity of 2 MW. His textile facility is operating below capacity and he has long wanted to sell electricity to nearby companies to generate additional revenue, but the required surcharge made it unprofitable. He told us, however, that he should now be able to do so profitably.

¶15. (SBU) Comment: Environmentally conscious observers may cringe at the prospect of hordes of private producers generating electricity inefficiently with relatively small diesel- and heavy fuel oil-powered generators, but the shortfall in electricity in the state is so acute that such concerns receive scant attention by policy makers. End Comment.

¶16. (U) Visit New Delhi's Classified Website:
http://www.state.sgov/p/sa/newdelhi

MULFORD